From: David Clendaniel [dclendaniel@doverfcu.com]
Sent: Monday, April 06, 2009 3:11 PM
To: _Regulatory Comments
Subject: David Clendaniel Comments on Advanced Notice of Proposed Rulemaking for Part 704

April 6, 2009

Mary Rupp, Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

Dear Ms Rupp:

It is quite evident that the current corporate credit union structure is outdated, poorly managed and inadequately supervised by regulators. These issues lead to the situation as it is now that will ultimately be paid by the 90 million credit union members nationwide. What accountability and liability does the Management and Directors of Corporates, as well as the National Credit Union Administration (NCUA) have? These parties have demonstrated on numerous occasions that they do have the expertise to manage these complex institutions. NCUA has also proven their lack of knowledge and capacity to adequately govern corporate credit unions to date. Any changes must first address these core issues before the other items can be addressed.

The current three tier system concentrates far too much risk with one entity and should never be replicated. This system allows for the unjust transfer of risk to natural person credit unions that is now taking place. How does NCUA expect natural person credit unions to continue to do business with institutions with failing capital and failing grades by the rating agencies? Are they to ignore their due diligence requirements at NCUA's verbal reassurance that it is going to be okay?

Payment System

Payment services should be a contractual relationship between entities and not be subject to capital deposits or other such requirements. Whether this is done through charter or regulatory changes is immaterial. The key is that a safe and separate payment system must exist to provide reliable service for credit union members.

Liquidity and liquidity management

Providing liquidity is a cornerstone for a financial services provider. However, in today's marketplace, corporate credit unions are not the only provider of this service and one must wonder if this is function is needed in corporates. Without the pertinent data available it is difficult to determine what caused the corporate failings. However, one must conclude that serious asset liability management (ALM) mistakes were made by chasing higher returns and failing to have adequate liquidity levels for the daily operations. Therefore, it is recommended that each surviving corporate credit union establish and maintain a threshold of liquidity that is applicable to the needs of their members. Any component of liquidity that relies on the liquidation or selling of investments to meet the established liquidity threshold must be severely discounted "shocked" to determine its adequacy. There should be a requirement that the oversight of this function be outsourced to a qualified third party provider.

Field of Membership Issues

One could argue that increased competition due to nationwide fields of membership was a factor in the current crisis. I do not agree with that argument. In fact a diversified field of membership may provide greater stability to a corporate credit union by eliminating location risk. Again, the current problem stems from inadequate management. It is the obligation of the Management of a financial institution to maintain its safety and soundness. Therefore failure rests with management not the fields of membership.

I cannot help but to wonder if there is a need for twenty eight (28) corporate credit unions to service the less than 8,000 credit unions nationwide. Contraction of corporate credit unions is an absolute.

Expanded Investment Authority

It would appear that by itself the misuse of the expanded investment authority is a contributing cause of the current corporate failures. The problem came from those corporate credit unions that chased higher yields without adequate knowledge, capital and internal controls. It would also be safe to assume that there was a lack of understanding by the Board of Directors of these institutions permitting these errors. Finally, there is inadequate knowledge, experience and capacity within the regulator (NCUA) to adequately assess the risks that these investments pose. Therefore, if this expanded investment authority is to stay, there must be established guidelines for adequate and professional oversight of these corporate credit unions. This oversight can be accomplished through a number of methods, such as creating minimum qualifications for the Board of Directors or contracting with firms that have the required expertise. NCUA must contract with a third party to perform their oversight role. Additionally, corporate credit unions that create a business model that assumes greater risk must be required to have greater capital. In other words implement a Risk Based Capital regulation.

Structure; two-tiered system

As stated previously the three tier system must be eliminated. It is my belief that systems should not be created by law. Rather it should occur as a facet of free enterprise. Going forward, it is an absolute that natural person credit unions receive fully audited financial statements from their corporate credit union, and those other entities, credit union or bank, to provide added details on the investments in their portfolio.

Core capital

There must be an adequate limit of core capital required for corporate credit unions. Core capital must only consist of undivided earnings. This level should be no less than 5%.

Membership capital

Membership capital should not be used to bind two institutions together for any length of time. That is a matter for contractual law. Since we are discussing credit unions, there should be a requirement for membership shares. However, these “required” shares cannot be used as a means to establish or increase capital.

Risk-based capital and contributed capital requirements

Risk based capital must be implemented for corporate credit unions.

Permissible Investments

The investment powers of corporate credit unions should exceed those of natural person credit unions. However, this power must be exercised with proper checks and balances and be maintained by those with adequate knowledge and experience. They must also be regulated and examined by those possessing sufficient knowledge to comprehend the complexities of the permitted investments.

Credit Risk Management

NCUA should require more than one rating for an investment and require that the lowest rating meet the minimum rating requirements of Part 704. Again, given the greater investment powers, corporate credit unions should be required to conduct additional stress modeling of investments.

Asset Liability Management

NCUA should require corporate credit unions to perform net interest income modeling and stress testing.

Corporate Governance

There must be minimum qualifications and training requirements for directors of corporate credit unions. This would ensure a director possess an appropriate level of experience and independence to comprehend the inherent risks in the investment portfolio. Term limits is a good succession tool, but may require the use of “outside” directors.

Sincerely,

David W. Clendaniel, CCE
President/CEO
Dover Federal Credit Union